

## INFORMED BUDGETEER

### APPROPRIATIONS SCORECARD, WITH A MONTH LEFT

- It's hard to objectively measure the progress of completing the 13 appropriation bills for 1999, but let's try. One conference report, for Military Construction, has been completed and should be cleared for the President's signature as one of the first actions by the Senate upon its return from the August recess.
- Six bills have been passed by both the House and Senate and have entered the conference stage--Agriculture, Defense, Energy and Water, Legislative Branch, Transportation, and VA-HUD. In addition, the Senate has passed the Commerce-Justice-State bill and was just about to pass the Treasury-Postal bill when it was put off to be the first item for Senate consideration at the conclusion of the August recess. While, the House has passed the Interior bill, the number of likely amendments facing that bill in the Senate forestalled its consideration on the floor until September.

| Comparison of Appropriations Bills in House & Senate<br>(FY1999, \$ in millions) |         |         |         |         |                         |        |
|--|---------|---------|---------|---------|-------------------------|--------|
|  | Senate  |         | House   |         | Difference <sup>A</sup> |        |
|  | BA      | OT      | BA      | OT      | BA                      | OT     |
| <b>Ag</b>  |         |         |         |         |                         |        |
| non-def  | 13,698  | 14,069  | 13,596  | 14,031  | 102                     | 38     |
| <b>Commerce</b>  |         |         |         |         |                         |        |
| def  | 335     | 320     | --      | --      | NA                      | NA     |
| non-def  | 26,775  | 26,285  | --      | --      | NA                      | NA     |
| <u>crime</u>   | 5,514   | 4,688   | --      | --      | NA                      | NA     |
| total  | 32,624  | 31,293  | --      | --      | NA                      | NA     |
| <b>Defense</b>   |         |         |         |         |                         |        |
| def  | 250,290 | 244,942 | 250,499 | 247,408 | -209                    | -2,466 |
| <u>non-def</u>   | 27      | 27      | 27      | 27      | --                      | --     |
| Total  | 250,317 | 244,969 | 250,526 | 247,435 | -209                    | -2,466 |
| <b>DC</b>  |         |         |         |         |                         |        |
| non-def  | 482     | 481     | --      | --      | NA                      | NA     |
| <b>Energy</b>  |         |         |         |         |                         |        |
| def  | 12,030  | 11,818  | 11,934  | 11,771  | 96                      | 47     |
| <u>non-def</u>   | 8,912   | 8,896   | 8,719   | 8,742   | 193                     | 154    |
| total  | 20,942  | 20,714  | 20,653  | 20,513  | 289                     | 201    |
| <b>For. Ops.</b>   |         |         |         |         |                         |        |
| non-def  | 12,544  | 12,595  | --      | --      | NA                      | NA     |
| <b>Interior</b>  |         |         |         |         |                         |        |
| non-def  | 13,404  | 13,959  | 13,371  | 13,956  | 33                      | 3      |
| <b>Labor</b>   |         |         |         |         |                         |        |
| non-def  | --      | --      | --      | --      | --                      | --     |
| <u>crime</u>   | --      | --      | --      | --      | --                      | --     |
| total  | --      | --      | --      | --      | --                      | --     |
| <b>Leg branch</b>  |         |         |         |         |                         |        |
| non-def  | 2,361   | 2,333   | 2,330   | 2,302   | 31                      | 31     |
| <b>Mil. Con.</b>   |         |         |         |         |                         |        |
| def  | 8,450   | 9,185   | 8,450   | 9,185   | --                      | --     |
| <b>Transp.</b>   |         |         |         |         |                         |        |
| def  | 300     | 300     | 300     | 300     | --                      | --     |
| non-def  | 11,630  | 13,349  | 11,638  | 13,347  | -8                      | 2      |
| highways   | --      | 21,885  | --      | 21,885  | --                      | --     |
| <u>mass transit</u>  | 1,113   | 4,401   | --      | 4,401   | 1,113                   | --     |
| total  | 13,043  | 39,935  | 11,938  | 39,933  | 1,105                   | 2      |
| <b>Treasury</b>  |         |         |         |         |                         |        |
| non-def  | 13,214  | 12,073  | 13,209  | 12,428  | 5                       | -355   |
| <u>crime</u>   | 132     | 125     | 132     | 129     | --                      | -4     |
| total  | 13,346  | 12,198  | 13,341  | 12,557  | 5                       | -359   |
| <b>VA-HUD</b>  |         |         |         |         |                         |        |
| def  | 131     | 127     | 130     | 126     | 1                       | 1      |
| <u>non-def</u>   | 69,855  | 80,653  | 70,899  | 80,373  | -1,044                  | 280    |
| total  | 69,986  | 80,780  | 71,209  | 80,499  | -1,043                  | 281    |
| <b>TOTAL</b>   |         |         |         |         |                         |        |
| def  | 271,536 | 266,692 | 271,183 | 268,664 | 223                     | -2,098 |
| non-def  | 172,912 | 184,720 | 62,890  | 64,833  | 39,124                  | 39,514 |
| crime  | 5,646   | 4,813   | 132     | 129     | 5,514                   | 4,684  |
| highways   | --      | 21,885  | --      | 21,885  | --                      | --     |
| <u>mass transit</u>  | 1,113   | 4,401   | --      | 4,401   | 1,113                   | --     |
| total  | 450,094 | 456,225 | 405,233 | 414,125 | 44,861                  | 42,100 |

<sup>A</sup>Senate bill greater (+) or less than (-) House. SOURCE: SBC Majority staff.

- The several remaining bills face difficulties in funding or amendments or both that have required most work on them to be deferred until September: DC and Foreign Operations--reported only in the Senate, and Labor-HHS--reported only in the House.

- The table above shows that the bills with the most significant differences that have to be worked out between the House and Senate are primarily Defense, followed with somewhat smaller differences by Energy and Water, VA-HUD, and Treasury-Postal.

### THE ECONOMIC EFFECTS OF FEDERAL SPENDING ON INFRASTRUCTURE -- NOT GOOD!

- Congress gets so caught up with passing authorizing legislation and appropriating monies that it many times fails to ask the basic question: will this spending make any difference to the economy?

- Along comes a CBO study in June -- after the passage of the Transportation Efficiency Act for the 21th Century (TEA21) -- that addresses this question not only for federal infrastructure programs, but for other federal investments in such things as education and training, research and development. The report, prepared in response to a request from Senate Budget Committee, Chairman Pete Domenici; *The Economic Effects of Federal Spending on Infrastructure and Other Public Investments*, June 1998, and is available on the CBO's World Wide Web site.

- CBO's bottom line is that increased federal spending on investments in infrastructure, education and training, and research and development would be unlikely to have a perceptible effect on economic growth.

- Why? The conclusion rests in part on the observation that many federal investments have little net economic benefit -- either because they are selected for political or other noneconomic reasons or because they displace private-sector or state and local investments that would have occurred anyway.

- Federal spending can even reduce growth: when it displaces investment that is more productive, when it leads others to defer investments in the hope of getting federal funds, or when its full costs (including opportunity costs) exceed its benefits.

- For federal highway and infrastructure investments -- the report concludes that: some investments can be justified by their benefits to the economy, but such investments are few some and perhaps a substantial portion of federal spending in this area merely displaces what would have been done at the state or local level, and on balance available studies do not support the claim that increase in federal infrastructure spending would increase economic growth.

- For federal education and training investments, while such spending in the past increased productivity of U.S. workforce, the CBO study concludes it is "not clear that increases in spending on those activities by the federal government would lead to additional growth." Many of the federal education and training programs target social goals, such as educational opportunity, rather than workforce productivity.

- For federal investment in R&D three conclusions were reached: (1) most federal R&D is mission oriented and typically cannot be justified by its economic returns, (2) academic research, such as NSF and NIH has provided society with substantial return, and some applied research, most notably in agriculture and health, has also more than paid for itself, and (3) nevertheless, funding increases in these areas may not produce returns as high as those seen at current funding levels.

- The bottom line, while some federal investments may not be justified on economic grounds, funding may be justified for other social objectives, e.g. economic opportunity. But there is ample reason to be skeptical that increased federal investment spending beyond its current level of about \$170 billion in 1997 or 2% of GDP, will increase the growth of GDP.

### STATE RANKINGS: FEDERAL EXPENDITURES

## TO SEQUESTER OR NOT TO SEQUESTER

- The Tax Foundation recently released its annual report on state-by-state federal taxes and expenditures, including ratios of federal expenditures per dollar of federal taxes collected in each state.

| <b>FEDERAL EXPENDITURES PER DOLLAR OF TAXES</b> |                                 |                             |                         |
|---|---------------------------------|-----------------------------|-------------------------|
|   | Ratio                           | Percent of National Average |                         |
|   | Expenditures<br>per \$ of Taxes | Federal<br>Taxes            | Federal<br>Expenditures |
| <b>Top 5 States</b>                             |                                 |                             |                         |
| New Mexico                                      | 1.89                            | 72                          | 136                     |
| North Dakota                                    | 1.62                            | 79                          | 128                     |
| West Virginia                                   | 1.61                            | 68                          | 109                     |
| Mississippi                                     | 1.58                            | 67                          | 105                     |
| Montana   | 1.48                            | 74                          | 110                     |
| <b>Last 5 States</b>                            |                                 |                             |                         |
| New Hampshire                                   | 0.73                            | 112                         | 82                      |
| Illinois  | 0.73                            | 117                         | 85                      |
| Nevada  | 0.73                            | 113                         | 82                      |
| New Jersey                                      | 0.69                            | 137                         | 94                      |
| Connecticut                                     | 0.67                            | 156                         | 104                     |

- Not surprisingly, states with low per capita tax burdens and/or high per capita expenditures benefit the most from federal fiscal operations and vice versa. For example, New Mexico's federal tax burden was 72% of the national average, while its expenditure level was 136% of the national average. Connecticut's tax burden, on the other hand, was 156% of the national average, while its expenditure level was 104% of the national average.

### TAX FACTS

- The average federal individual income tax rate was the same in 1985 and 1995, 13.9%. The total figure indicates that federal income tax policy has not changed much -- but that's not the case. Between 1985 and 1991 the average federal income tax rate fell more than a percentage point, but rose to its 1985 level by 1995.
- Taxpayers in the upper half of the adjusted gross income scale (\$22,344 in 1995) saw their average income tax rate fluctuate over the past decade, while taxpayers in the bottom 50% saw their average income tax rate steadily decline. Taxpayers in the top half paid more than 95% of federal income tax in 1995, a figure that has increased slowly but steadily since 1985.

| <b>INDIVIDUAL FEDERAL INCOME TAX FACTOIDS</b> |                            |                   |            |               |                  |               |
|---|----------------------------|-------------------|------------|---------------|------------------|---------------|
| Year  | # of Returns<br>(millions) | Average Tax Rates |            |               | Income Tax Share |               |
|   |                            | Total             | Top<br>50% | Bottom<br>50% | Top<br>50%       | Bottom<br>50% |
| 1985  | 100.6                      | 13.9              | 15.6       | 5.7           | 92.9             | 7.1           |
| 1986  | 102.1                      | 14.5              | 16.3       | 5.6           | 93.5             | 6.5           |
| 1987  | 106.2                      | 13.1              | 14.6       | 5.1           | 93.9             | 6.1           |
| 1988  | 108.9                      | 13.2              | 16.6       | 5.1           | 94.3             | 5.7           |
| 1989  | 111.3                      | 13.1              | 14.5       | 5.1           | 94.2             | 5.8           |
| 1990  | 112.8                      | 12.9              | 14.4       | 5.0           | 94.2             | 5.8           |
| 1991  | 113.8                      | 12.8              | 14.2       | 4.6           | 94.5             | 5.5           |
| 1992  | 112.7                      | 12.9              | 14.4       | 4.4           | 94.9             | 5.1           |
| 1993  | 113.7                      | 13.3              | 14.9       | 4.3           | 95.2             | 4.8           |
| 1994  | 115.0                      | 13.5              | 15.1       | 4.3           | 95.2             | 4.8           |
| 1995  | 117.3                      | 13.9              | 15.5       | 4.4           | 95.4             | 4.6           |

Source: Statistics of Income Bulletin, volume 17, number 4; p. 35-38.

### **BUDGET QUIZ**

**QUESTION:** In what circumstances could a sequester occur at the end of this fiscal year?

**ANSWER:** Unlike Hamlet, informed budgeteers do not need to philosophize about sequestration. They know that sequestration is the reduction of nonexempt accounts by a uniform percentage to meet statutory budget goals. For discretionary spending, a sequester would occur if OMB estimates that appropriated spending exceeds the statutory limits for the different categories of defense, nondefense, and crime. The recently enacted TEA-21 exempts its highway and mass transit cap spending from sequestration, although any overage would be charged against the nondefense limit and could trigger a sequester.

For direct spending and revenues, OMB is required to estimate the on-budget deficit impact of all legislation (except deposit insurance) enacted since the adoption of the 1997 reconciliation bills. If the sum of such legislation causes an increase in the on-budget deficit, all nonexempt direct spending accounts will be reduced by sequestration. Unlike discretionary programs, most direct spending is exempt (like welfare or retirement programs) or subject to special rules (like medicare). A sequestration order does not affect revenues.

**BONUS QUESTION:** In what cases could a sequester be waived?

**BONUS ANSWER:** One way around the sequester issue is to have Congress pass a joint resolution that waives the sequester mechanism due to war or low growth. However, both latter events are very unlikely right now (fortunately!). Some inquiring budgeteers may wonder if the second quarter slowdown could constitute a period of "low growth". It does not. CBO only issues a "Low Growth Report" after either of two conditions are met: 1) CBO forecasts that there will be two consecutive quarters of negative growth sometime during the next six quarters; or 2) the Commerce Dept. reports two consecutive quarters with less than 1 percent growth.

At present, neither "Low Growth" condition is met: 1) CBO is not forecasting two consecutive quarters of negative growth during the budget window. CBO expected a sharp slowdown in the second quarter, but looks for growth to pick up again in the second half. 2) Second quarter GDP growth came in just above 1%. While it's always possible that this could be revised later, it seems very unlikely that we will see two, consecutive sub-one percent growth quarters this year given the positive fundamentals underlying the US economy.

Lastly, the transmission of a "Low Growth Report" is no guarantee that Congress will actually vote to waive Gramm-Rudman-Hollings enforcement mechanisms. During the depths of the 1991 recession, the Senate voted resoundingly against overturning these mechanisms. As for war, there's always Canada.

### **QUOTE OF NOTE**

**How will you ever convince the American people of that, since they always believe the government would mess up a two-car parade? I mean, even if you're right, politically, how do we ever -- how do you make that sale to the American people?**

President Clinton, discussing having the government invest and manage Social Security funds; July 27, 1998, Albuquerque, New Mexico; The Great Social Security Debate #3.

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| <p><b>Editor's Note:</b> This will be the last <i>Bulletin</i> until Congress reconvenes in Septemeber. After the August recess break, informed budgeteers can expect a new <i>Bulletin</i> the week of September 8.</p> |
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